Coalition Ex. 2.0

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

COMMONWEALTH EDISON COMPANY,	)	
	)	
Petition for Approval of a Revision to Decommissioning Expense Adjustment Rider to Take Effect on Transfer of ComEd's Generating Stations	)	Docket No. 00-0361

REBUTTAL TESTIMONY OF
EDWARD C. BODMER
ON BEHALF OF
CITGO PETROLUEM CORP., GENERAL MILLS, INC.,
THE METROPOLITAN CHICAGO HEALTHCARE COUNCIL,
AND R.R. DONNELLEY & SONS COMPANY

DATED: August 14, 2000

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REBUTTAL TESTIMONY OF EDWARD C. BODMER

Q. Are you the same Edward C. Bodmer who presented direct testimony in the instant proceeding?

A. Yes. I am again testifying on behalf of Citgo Petroleum Corp., General Mills, Inc., the Metropolitan Chicago Healthcare Council and R. R. Donnelley & Sons Company (collectively the "Industrial and Health Care Customers Coalition" or the "Coalition").

I.
SUMMARY OF RECOMMENDATIONS

Q. Please summarize the recommendations in your direct testimony.

A. The Illinois Commerce Commission ("Commission") should reject or substantially modify the proposal submitted by Commonwealth Edison Company's ("Edison"). If Edison is allowed to transfer its nuclear generation assets to Exelon Genco, then the Commission should either:

(1) order Edison to hold a bid auction for its decommissioning liability and its decommissioning funds; or

(2) develop an allocation methodology that attributes a fair share of the decommissioning costs to Exelon Genco and trues-up ratepayer contributions for decommissioning costs through refunds as new information arises.

Alternatively, if the Commission accepts the structure of Edison's proposal, the up-front, increased ratepayer charges proposed by Edison should be eliminated. Edison's proposed increase in the rates to be paid for decommissioning would be unjust and unreasonable, and would be an unnecessarily heavy burden upon customers.

Q. What is the purpose of your rebuttal testimony in this proceeding?

A. My rebuttal testimony responds to the direct testimony submitted by the Attorney General of the State of Illinois ("AG"), City of Chicago/Citizens Utility Board ("City/CUB"), Illinois Industrial Energy Consumers ("IIEC"), NewEnergy Midwest, L.L.C. ("NewEnergy"), and the Staff of the Illinois Commerce Commission ("Staff"). My testimony also responds to the August 1, 2000 direction of the Hearing Examiners suggesting that parties respond to the Questions submitted by Commissioner Kretschmer. My testimony responds to some of the questions that are not directly related to Edison management decisions and do not call for legal arguments, conclusions, or interpretations.

II.

RESPONSE TO STAFF AND INTERVENOR DIRECT TESTIMONY

Q. Does the testimony submitted by the AG, City/CUB or the IIEC conflict with your direct testimony?

A. No. Generally, the witnesses for these organizations demonstrate that under its decommissioning proposal, Edison has the potential to **over collect** money from ratepayers relative to actual ultimate decommissioning costs. These witnesses advocate positions similar to my recommendation relating to zero up-front payments if the

structure of Edison's proposal is adopted. With the exception of IIEC[1], these witnesses reach this conclusion without allocating any costs to Exelon Genco. In other words, these witnesses reached the conclusion that Edison is not entitled to any further up-front ratepayer contributions even assuming that 100% of decommissioning costs were allocated to ratepayers and none to Exelon Genco.

The witnesses for the AG, City/CUB, and IIEC each note many reasons that decommissioning costs may be lower than Edison's estimates. These reasons include, but are not limited to, delays in decommissioning outlays caused by license extensions, reduced funding for site restoration, lower contingency factors, lower escalation rates, higher real earnings rates on the decommissioning fund, economies of scale, and technological improvements. (*See generally*, AG Witness David J. Effron Direct Testimony; City/CUB Witnesses Bruce E. Biewald and David A. Schlissel Direct Testimony; IIEC Witness Robert R. Stephens Direct Testimony.) The City/CUB witnesses support their position in part by pointing out that Amergen's cost estimate for decommissioning the Vermont Yankee plant is dramatically lower than the decommissioning estimate that TLG presented to the Vermont Public Service Board for the same plant. (*See* City/CUB Witness Schlissel Direct Testimony at 28-29; City/CUB Witness Biewald Direct Testimony at 11-12.)

[1] IIEC witness Mr. Robert Stevens implies that decommissioning costs should be allocated to Exelon Genco when he states at page 16 of his direct testimony that "there is no compelling indication from ComEd that the Genco would need any further decommissioning contributions from ComEd customers for any period of time, given the potential margins available from the output of the nuclear units." (page 16, lines 10-13).

Q. Please explain how the information presented by the intervenors' witnesses relates to the "negotiating dilemma" that you discussed in your direct testimony.

A. As discussed in my direct testimony at pages 6-7, the Commission and Edison's ratepayers are being asked to give up their statutory right to wait and see what the actual decommissioning costs turn out to be. By giving up this right, ratepayers are faced with a "negotiating dilemma." Complicating matters is the fact that decommissioning costs are uncertain, Edison has far more information concerning actual ultimate decommissioning costs than ratepayers, Edison's proposal will not affect the actual activities associated with decommissioning its plants, and Edison has a very strong incentive to assure that funding is adequate.

In this context, the information presented by witnesses for the AG, City/CUB, and the IIEC confirms that there is a significant probability that the ultimate level of decommissioning costs may be significantly lower than estimated by Edison in the instant proceeding. AG witness Mr. David Effron noted Edison's skewed incentives regarding decommissioning funding:

> [I]t is understandable that ComEd would sincerely prefer that any potential error be on the side of over-funding rather than under-funding. Ideally, from the perspective of ComEd, the possibility of under-funding should be eliminated. However, the only way to achieve such a goal is to adopt overly conservative assumptions in calculating the amounts necessary to provide for decommissioning.

(*See* AG Witness Effron Direct Testimony at 23.) The witnesses for the AG, City/CUB, and IIEC demonstrated the potential likelihood of ratepayers over-funding Edison's decommissioning obligations. These demonstrations support the Coalition's recommendation for an auction for decommissioning obligations; an allocation

methodology that attributes a fair share of the decommissioning costs to Exelon Genco; and a true-up of ratepayer contributions for decommissioning costs as new information arises.

Q. Please comment upon the recommendation made by the Commission Staff that ratepayers pay $78.9 million per year of additional decommissioning funding over the next four years?

A. Staff witness Mr. William Riley recommends that decommissioning costs should be reduced relative to Edison's proposal, and that ratepayer funding be tied to contractual arrangements between Exelon Genco and Edison. For example, on page 2, line 40 of his direct testimony, Mr. Riley states: "The collection period should be shortened from six to four years to be consistent with the required period of the purchase power agreement (PPA) between Exelon Genco and ComEd." In contrast, I demonstrated in my direct testimony that the focus of allocating decommissioning costs between Exelon Genco and ratepayers is the time period in which the plants are subject to market forces rather than the time period over which the plants are implicitly being subject to rates derived from regulatory formulas – either frozen rates or transition charges. As a result, and contrary to Mr. Riley's conclusions, my approach demonstrates that no added ratepayer contributions are necessary.

Q. Do any other witnesses address the appropriate time period for collection of additional decommissioning funds from ratepayers?

A. Yes. IIEC Witness Stephens finds **no logical support** for Edison's proposed six year continuing collection period or any other time period. (*See* IIEC Witness Stephens Direct Testimony at 11.) (Emphasis added.) While noting that the four year limitation on continued collections may have superficial appeal due to its correspondence with the PPA, Mr. Stephens correctly notes that it is Exelon Genco or Edison that gets the benefit of low incremental cost nuclear generation during this period. (*See id.*)

Q. Please explain the difference between your recommendation and Staff Witness Riley's suggestion.

A. The primary difference between Staff witness Riley's suggestion and my recommendation is that Mr. Riley suggests ratepayers continue to make payments to the decommissioning trust funds under the structure of Edison's proposal. As I discussed in my direct testimony at page 23, to evaluate alternative allocation assumptions between captive ratepayers and Exelon Genco, it is appropriate to split the present value of decommissioning contributions into three "pots," using Edison's own data. The first "pot" is the current value from ratepayer contributions of the decommissioning trust as of January 2000. (*See id.*) The second "pot" is the present value to the year 2000 of the amount that Edison is requesting from ratepayers through the end of 2006. (*See id.*) The third "pot" is the present value to 2000 of the amount that supposedly would be the responsibility of Exelon Genco under Edison's proposal. (*See id.*)

Q. What would be the financial impact of the Commission accepting Mr. Riley's suggestion?

A. If ratepayers pay $78.9 million over four years as suggested by Staff witness Riley, and if Edison's decommissioning funding projections presented in its response to CUB Data Request No. 11 turn out to be true, ratepayers will pay 83% of the plant costs and Exelon Genco will pay only 17% of the costs, even though between 30% to 42% of the lifetime of the plants, depending on the length of the license, will be subject to unregulated profits as a result of Exelon Genco's ownership of the plants. This is illustrated in the table below:

Present Value (Year 2000) of Decommissioning Funding and Plant Age					
	$ Millions	Percentage Of Recovery	Percentage of Plant Life without License Extension	Percentage of Plant Life with ½ License Extension of 10 Years	Percentage of Plant Life with License Extension of 20 Years
Pot 1: Ratepayer Funded before 2000	$2,654.36	73.7%			
Pot 2: Ratepayer Funding 2000-2004	$ 324.64	9.0%			
Pot 3: Funding After 2004	$ 622.18	17.3%			
Total Ratepayer	$2,979.00	82.7%	70.1%	63.3%	57.7%
Total Genco	$ 622.18	17.3%	29.9%	36.7%	42.3%
Total	$3,601.18	100.0%	100.0%	100.0%	100.0%

Q. Are the figures used in this table the same as those that appeared in your direct testimony?

A. The numbers in this table are derived slightly differently than in my direct testimony because the numbers used in this table include the $71.7 million transfers if pre-1989 collections that account for ratepayer contributions before the external funds were established. The present value of this amount -- $53 million should be included in "Pot 1."

Q. Please respond to the direct testimony submitted by NewEnergy witness Dr. O'Connor?

A. NewEnergy witness Dr. O'Connor makes an articulate contention that an alternative method of allocating risks associated with decommissioning cost estimates is good public policy and that Edison's proposal is favorable from a competitive perspective. While I agree that an approach different than Rider 31 should be sought for the treatment of decommissioning cost, and that ratepayers are not efficient bearers of risk, Edison's proposal is not the appropriate fix. Similarly, the risk allocation features emphasized by Dr. O'Connor (whereby Exelon Genco accepts risks of decommissioning cash outflows being different from levels that are currently expected) will occur whether the "up-front" payment is $121 million or zero. In fact, many of Dr. O'Connor's reasons for supporting Edison's proposal do not appear to be based upon any of the details contained within Edison's proposal.

Q. How does NewEnergy Witness Dr. O'Connor's recommendation compare with your recommendation that a bid auction be held for Edison's decommissioning liabilities?

A. As discussed in my direct testimony at page 10, the Commission could order Edison to put its future decommissioning work as well as the accumulated amounts in decommissioning trust funds up for auction. This means that Edison would allow other companies to perform the decommissioning work, take over the decommissioning trust funds and accept the risk that decommissioning costs will vary from the current expected levels. My proposal to hold a bid auction for Edison's decommissioning liability and

decommissioning funds is an extension of Dr. O'Connor's recommendation that risks should be allocated.

Q. NewEnergy witness Dr. O'Connor makes the statement that "given the inability to pass on increased decommissioning costs, Edison's nuclear Genco or its successor would be placed on a more even footing with other sources of generation since the artificiality of externalizing a risk that ought to be internalized will have been eliminated." Do you agree with Dr. O'Connor?

A. No. Through its amortization policies and because of the general method by which stranded investment is recovered under the lost revenue approach in the Public Utilities Act, Edison will have an artificially strong competitive position even if Exelon Genco pays its fair share of decommissioning costs. As explained in my direct testimony at page 35, once it is truly subject to market forces, the generating subsidiary will have the realistic potential for **operating profit of more than $1 billion per year** on an investment base that is initially in the $2-3 billion range and declines thereafter. As discussed more fully below, allocating a fair share of decommissioning costs to Exelon Genco would only add about $1.34/MWH to the generating costs – relative to market prices that have been in the $40/MWH range.

Q. How will Edison's proposal impact the competitive generation market in Illinois?

A. Contrary to NewEnergy witness Dr. O'Connor's assertions, rather than creating a level playing field, Edison's proposal likely will result in market structure problems that favor its own nuclear plants. Edison will be able to compete with a fleet of assets that have

relatively low book value combined with very low and stable fuel costs. This cost structure together with its size in the market will potentially allow Exelon Genco to operate in some monopolistic or oligopolistic ways. The Commission should be mindful not to further aggravate a potential market power problem by granting Edison and its unregulated subsidiary even more financial advantages. By failing to allocate a portion of Edison's decommissioning liability to Exelon Genco, the Commission will have failed to act to promote the development of the competitive market in Illinois.

Q. Please comment upon whether any of the Staff and Intervenor witnesses addressed the rate impacts of Edison's proposal.

A. No other witnesses performed an analysis of how Edison's proposal would specifically impact the electric bills paid by ratepayers. IIEC witness Stephens correctly notes that large consumers of energy would be among those customers hardest hit by the increase in collections proposed by Edison. (*See* IIEC Witness Stephens Direct Testimony at 2.) As I stated in my direct testimony at page 4, the electric bills of the Coalition members would change by sizable dollar amounts depending on the course of action chosen by the Commission. For example, for some large customers, Edison's proposal would result in a **$250,000 per year rate increase**. A manufacturing customer consuming 8 million kWh per month would experience approximately a **$43,000 per year rate increase**. The electric bill of a typical hospital would **increase by $15,000 annually** if Edison's proposal were adopted.

III.

<u>RESPONSE TO COMMISSIONER KRETSCHMER'S QUESTIONS</u>

Q. In his response to my eleventh question, Mr. Berdelle stated that "the Genco will have additional flexibility to manage fund investments to maximize risk-adjusted earnings and to make contributions to trust funds at appropriate times." ComEd Ex. 6 at 14. What additional flexibility and control over the timing of contributions will Exelon Genco have that ComEd does not? What is the expected benefit (in 2000 dollars) of such flexibility and control?

A. As I discussed in my direct testimony at page 16, increased decommissioning trust fund earnings from a higher proportion of equity funding comes only at the expense of accepting increased risk. (*See* Coalition Witness Bodmer Direct Testimony at 16.) Since the ultimate physical decommissioning of all of Edison's plants will not be finished for almost half a century, the possibility that Exelon and/or Edison and/or PECO will not exist as solvent corporate entities must be considered from a public policy perspective. This means that accepting greater risk involves public policy considerations because citizens of Illinois would be left holding the bag if Exelon and Edison are bankrupt. Similarly, if an investment strategy conducted by Exelon Genco is good, a similar strategy conducted under the ratepayer protections contained under the current Rider 31 structure must also be good. Edison's proposal to move assets from one subsidiary company to another is simply a "shell game" that has nothing to do with optimal investment strategies from either an efficiency perspective or from a public policy perspective.

Q. In his response to my eleventh question, Mr. Berdelle notes that "market prices for energy" will be a source of "potential profitability" for Genco that will offset its risk. ComEd Ex. 6 at 13. What are ComEd's market price expectations and how do these expectations minimize Exelon Genco's risk? Does ComEd expect that Exelon Genco will be able to recover some or all of the expected decommissioning costs through market rates?

A. By adjusting the data that Edison provided in response to CUB data request No. 11, I have computed the approximate impact upon the cash flows of Exelon Genco if it accepted some of the decommissioning funding obligations. This computation reveals that Exelon Genco could easily accept decommissioning financial obligations that result from an equitable allocation of costs because the decommissioning funding is only about 2.9% to 4.5% of the market price.

Q. Please explain your calculations.

A. The calculations are based upon Edison's assumptions with respect to the dollar level of decommissioning outflows that will ultimately be incurred to physically decommission the nuclear plants. The calculations reflect derived funding levels that Exelon Genco would have to incur if ratepayers do not make any further contributions to the decommissioning funds – i.e. no more "up-front payments." Furthermore, the calculations assume that Exelon Genco would make funding contributions from the year 2005 through the year 2020 escalating at a rate of 2%. The dollar funding level required by Exelon Genco is derived on the basis that it will provide the same ability to fund physical decommissioning activities as in the case where ratepayers pay $121 million

over six years. This dollar amount computed on this basis is $90 million in 2005 (and it escalates at a rate of 2% per year through the year 2020).

Edison has more than 9,000 MW in nuclear capacity. Operating at an 85% capacity factor, Edison can generate 67,014,000 MWH per year. The cost per MWH of a $90 million decommissioning funding obligation that Exelon Genco would incur is only $1.34/MWH. Relative to market prices in the $30-$45/MWH range, this $1.34/MWH cost is a relatively insignificant 2.9% to 4.4% of market prices. Given the low book value and the low fuel costs of Edison's nuclear plants, the Company does not need an artificial financial incentive to alleviate it of decommissioning obligations that cost only $1.34/MWH.

Q. Assuming that the operating lives of all six Braidwood, Byron and LaSalle units are extended and ComEd's Petition is granted, what will the balance of the funds be upon decommissioning? Assuming that the operating lives of the other units are extended and ComEd's Petition is granted, what will the balance of the funds be upon decommissioning?

A. Witnesses for the AG, City/CUB, IIEC, and Staff all described how Edison's asserted decommissioning funding requirement of $121 million could be significantly reduced because of extending the life of the nuclear plants. (See AG Witness Effron Direct Testimony at 20-22; City/CUB Witness Schlissel Direct Testimony at 2-5, 6-22; IIEC Witness Stephens Direct Testimony at 9-11; Staff Witness Riley Direct Testimony at 7-10.) If future performance is anywhere near the recent performance, the returns on the

fund will be dramatically more than Edison's assumptions. The reason for a reduced funding requirement is that the real interest rate on the trust funds exceeds the real levels of periodic storage costs. In other words, the benefits in terms of fund earnings exceeds the inflation increases and the increased storage costs.

In addition to the numerous effects of license extensions on reducing decommissioning costs that are described by the AG, City/CUB, IIEC, and Staff, the Commission should consider two added impacts that ought to reduce up front funding requirements if physical decommissioning is delayed.

Q. Please explain the first impact related to the yield curve on interest rates that the Commission should consider if actual decommissioning of Edison's nuclear plants is delayed.

A. The first impact is related to the yield curve on interest rates. Generally, the yield curve for interest rates is upward sloping which implies that funds invested for a longer time period earn a higher rate of return. Delay of decommissioning allows funds to be invested in longer-term securities and earn higher rates of returns on the ratepayer funded decommissioning balances.

Q. Please describe the second impact on the allocation of costs that the Commission should consider if decommissioning of Edison's nuclear plants is delayed.

A. The second impact is the allocation of costs between the Exelon Genco and captive ratepayers. As noted in my direct testimony at page 30, without any life extension,

earnings represent 30% of the life of the nuclear fleet from competitive prices. If there are no further up-front payments, and if Edison's cost estimates of physical decommissioning cash outlays turn out to be correct, Exelon Genco would be responsible for 17% of the decommissioning funding. However, if Edison operates the plants longer, more funding should be allocated to Exelon Genco. The allocation of decommission costs – 17% -- remains the same, but the percentage of plant life represented by competitive prices increases above 30%. This means that even if Edison's cost estimates are accepted, with extended operating lives on the plants, there should theoretically be ratepayer refunds based upon an equitable allocation approach.

Q. If persuasive "assurances" can be offered to the NRC and allegedly high risk levels can be accepted by Exelon and/or Exelon Genco, then it stands to reason that ComEd's ratepayers bear a significant risk of overpayment under ComEd's Petition. What can ComEd offer to assuage such concerns? Will ComEd agree to revise the Contribution Agreement to require Exelon Genco to refund any over recovery as each unit is decommissioned?

A. This question identifies one of the central concerns confronting both the Commission and ratepayers in this proceeding. To date, Edison has failed to provide adequate assurance that there will be no overpayment by ratepayers as a result of this proceeding. Since Edison has failed to address such concerns, my proposal to conduct a bid auction of Edison's future decommissioning could solve this difficult problem through the use of market forces. In order to win the auction, the bidders would have to accept a reasonable degree of risk that decommissioning cash outlays are either above or below projected

levels. If ratepayers are required to make **any** additional decommissioning payments, it would be unreasonable for ratepayers to give up their right to potential refunds.

Q. How else do you recommend to assuage such concerns regarding overpayment by ratepayers?

My other alternative to allocate a fair share of the decommissioning costs to Exelon Genco and true-up ratepayer contributions for decommissioning costs through refunds as new information arises protects ratepayers from the risk of over-funding. I emphasize that the issue of potential over-funding is not only relevant when physical decommissioning occurs, but that as time passes, the uncertainty around decommissioning will be lowered because of the experience (i.e., efficiencies) gained from more and more large plants being decommissioned.

Elsewhere in the country where decommissioning is occurring, utility company executives recognize that decommissioning funds belong to ratepayers rather than shareholders. An article titled "Decommissioning Trust Funds Lure Potential Nuclear Plant Buyers" published in Nucleonics Week quoted an executive from Portland General Electric: "PGE spokesman Kregg Arnston said …. If there is any money left over when decommissioning is done, currently scheduled for the end of 2002, the funds will be returned to ratepayers." The same article stated with respect to the Big Rock Plant in Michigan that: "any excess decommissioning funds will also be rebated to ratepayers, since the money came from them in the first place. 'It's not our money,' a Consumers

spokesman said. 'It's the ratepayers'." Thus, other states have recognized that ratepayers are entitled to refunds as a result of over collection of decommissioning funds.

Q. Given the possibility of license extensions, what impact will technological advancements have on decommissioning costs over the next fifty years?

A. As with production functions for other goods and services, more efficient business practices and technological innovations occur over time. This is the reason a productivity factor is used in price cap plans. While the pace of technological innovation and increased real efficiency is difficult to forecast, the same article that I quoted above from Nucleonics Week discussed the potential for increased efficiencies:

> The trust funds are made up of ratepayer contributions and investment income. While some anti-nuclear and environmental groups have argued for years that utilities won't have sufficient funds in their accounts to decommission their units – particularly if they are shut down early -- other observers maintain that the **funds will be more than sufficient, because decommissioning costs will drop as utilities and contractors become more efficient at cleaning up the sites. Major variables include federal standards for releasing sites for other uses and the cost of low-level waste disposal when a plant is dismantled**…. There are some people in the industry who think the decommissioning funds are grossly under funded. They don't want to have that risk. But others say 'Hey, the first couple of environmental cleanups (for so-called "Superfund" sites) were expensive, but the costs came down and they got smarter, new technologies developed and a competitive cleanup industry grew.

(Emphasis added.) Technological advances and experience in decommissioning other large-scale nuclear plants can only lead to greater efficiencies and reduced costs over time. Edison's assertions to the contrary fly in the face of common sense, logic, and the experience in other related areas.

IV.

SUMMARY OF RECOMMENDATIONS

Q. Please summarize your recommendations.

A. The Commission should reject or substantially modify Edison's proposal. As stated in my direct testimony at page 38, the Commission is faced with a significant threshold question in another docket regarding whether it should allow Edison to transfer its nuclear plants and decommissioning trust funds to an unregulated affiliate. If the Commission allows the transfer, the Commission must take the steps necessary to ensure that Edison's shareholders are not unduly enriched at the expense of its ratepayers.

The structure of Edison's decommissioning proposal is designed to unjustly enrich Edison's shareholders. Thus, my primary recommendation is that the Commission should reject the underlying structure of Edison's proposal. However, the Coalition has outlined two alternative structures for the Commission to consider in the instant proceeding: (1) an auction approach, under which Edison would auction the decommissioning trust fund along with the decommissioning liabilities; or (2) an up-front allocation of decommissioning costs between ratepayers and Exelon Genco with an annual true-up. Either of these structures would be a significant improvement upon Edison's proposal.

Q. Do you have any recommendations if the Commission approves the underlying structure of Edison's proposal?

A. Yes. If the Commission nevertheless approves the underlying structure of Edison's proposal, the Commission must make several important modifications. **First**, ratepayers should not be required to make any further decommissioning payments; they have already paid more than their fair share. **Second**, the Commission must ensure that Exelon Genco does not remove any money from the decommissioning trust funds until all of the plants are fully decommissioned. **Finally**, the Commission must ensure that Edison or its affiliates never come back for another bite of the apple; the Commission must ensure that there is no loophole that Edison can exploit.

Q. Does this conclude your testimony?

A. Yes.